IN THE

SUPREME COURT OF THE UNITED STATES

ATLANTIC COAST LINE RAILROAD COMPANY,
Appellant,

vs.

M. E. THOMPSON, STATE REVENUE
COMMISSIONER OF GEORGIA,
Appellee.

BRIEF FOR ATLANTIC COAST LINE RAILROAD COMPANY IN REPLY TO APPELLEE'S MOTION TO DISMISS OR AFFIRM.

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Appellee.

BRIEF FOR APPELLANT IN REPLY TO APPELLEE'S MOTION TO DISMISS OR AFFIRM.

The motion to dismiss or affirm is made under Rule 12, Par. 3. The motion is really an abuse of the Rule. The Rule contemplates that, when the Appellee files with the Clerk of the Court possessed of the record, any matter or ground making against the jurisdiction of this Court asserted by the Appellant, under those circumstances the Appellee may also file a motion to dismiss or affirm. The statement of the Appellee does not disclose any matter or ground against the jurisdiction of this Court: The jurisdiction of this Court rests on the ground that the Supreme Court of Georgia has upheld the validity of a Georgia Statute, which Statute is attacked on the ground that it is repugnant to the Contract Clause of the Constitution of the United States. Appellee merely asserts that there was no contract. That is the question in the case. If, on hearing

the case, it should turn out that there was no contract, this would not affect the jurisdiction of the Court; it would merely result in the Appellant losing its case.

The motion to dismiss or affirm is predicated on the proposition "that the questions on which the decision of the cause depends are so unsubstantial as not to need further argument" (Rule 7, Par. 4). The decision of the Supreme Court of Georgia demonstrates that the questions are not "unsubstantial". In order to reach its decision, the Supreme Court of Georgia, instead of following the interpretations which have heretofore been put by this Court on the Charter contract involved in this case, has worked out its own construction of the Charter contrary to the construction of this Charter by this Court. Furthermore, the decision of the Supreme Court of Georgia assumes that since this Court has construed the Charter, there has been a material change in the decisions of this Court applicable to the Charter.

In order to affirm the judgment of the Supreme Court of Georgia, this Court will have to completely reverse itself on its constructions of this Charter.

As under Rule 7 (3) Appellant must file its brief 20 days after service of Appellee's motion, and as the record has not been printed, the references herein are necessarily to the pages of the typewritten transcript of the record.

I

Statement of the Case.

Georgia Railroad and Banking Company leased its railroad properties to William M. Wadley in 1881 for 99 years at an annual rental of $600,000.00, and by

successive transfers Appellant and Louisville and Nashville Railroad Company eventually became the Lessees, each being the Lessee of a one-half interest in the leased property. (T.R. 61-68).

Section 15 of the Charter of Georgia Railroad Company (Acts 1833, p. 256), the name of which was changed to Georgia Railroad and Banking Company (Acts 1835, p. 181) provides:

> "The stock of said company and its branches shall be exempt from taxation for and during the term of seven years from and after the completion of the said railroads or any one of them; and after that, shall be subject to a tax not exceeding one-half percent per annum on the net proceeds of their investments." (T.R. 59)

This Charter provision is applicable only to the main line of railroad from Augusta, Ga., to Atlanta, Ga., and the branch from Union Point, Ga., to Athens, Ga. (T. R. 60). This provision of the Charter is hereafter referred to as the "Charter tax limitation", and the lines of railroad covered by it are hereafter referred to as the "Charter tax lines".

The power to lease is conferred by Sections 12 and 14 of the Charter (Acts 1833, pp. 256, 262, 263), a copy of which sections are attached hereto (Appendix 1).

The State Revenue Commissioner (the predecessor of Appellee), assessed against Appellant deficiency income taxes for the years 1941, 1942, and 1943, aggregating, with interest, about $200,000, the deficiency being the amount of one-half of the net income from

the operation of the Charter tax lines, the assessment being at the rate of 5½% on this net income (T.R. 63, 64).

The tax is assessed under the Income Tax Act of March 31, 1931, and amendments (Acts 1931, Ex. Sess. p. 94; Acts 1937, pp. 109, 117), now codified in the Annotated Code of Georgia, Section 92-3102, the material portion of which is as follows:

> "Every domestic corporation and every foreign corporation, shall pay annually an income tax equivalent to five and one-half per cent. of the net income from the property owned or from business done in Georgia as is defined in Section 92-3113." (T.R. 63).

The tax of one-half of 1% under said Section 15 of the Charter has been returned and paid on that basis for more than 100 years. (T.R. 95).

II

Contentions of Appellant.

The contentions of Appellant are set forth in the assignments of errors (T.R. 131), but for the purposes of this brief all that need be stated are the following:

1. The Charter tax limitation of the Georgia Railroad and Banking Company is an irrevocable contract protected from impairment by subsequent legislation by the Contract provision of the Federal Constitution (Art. 1, Sec. 10, Par. 1). (This question has been so thoroughly settled by the decisions of this Court hereafter referred to that it is unnecessary to discuss the

question in this brief. This question has also been settled by the Supreme Court of Georgia in *State of Georgia* v. *Georgia Railroad & Banking Co.*, 54 Ga. 424).

2. The thing taxed under the Charter is not the rentals received by the Lessor, it is the net income from the operation of the Charter Tax Lines, and this has been the practice for more than 100 years.

3. The tax is levied exclusively on the net income. No ad valorem tax can be assessed and the net income cannot be taxed higher than ½ of 1%.

4. The tax provisions of the Charter of the Georgia Railroad and Banking Company inure to the Lessees, and the demise of the property does not open up the Charter so as to permit the State to tax the Lessees with that which it could not tax the Lessor, as has been decided by this Court.

5. The Charter cannot be impaired by the device of defining the Charter tax as a tax on property (as the Supreme Court of Georgia has done), and then imposing on the Lessee a 5½% income tax.

6. The impairment of the contract is the same in substance, kind and extent, whether the tax imposed under Section 15 of the Charter is defined as a property tax or an income tax.

7. The tax imposed by Section 15 of the Charter is an income tax and not a property tax.

8. Railroads in Georgia were habitually taxed ½ of 1% on their net income until 1874, whether they had a Charter contract or not.

9. Rochester Railroad v. Rochester, 205 U.S. 236, and kindred cases, are held by this Court not to be applicable.

10. Hale v. State Board, 302 U.S. 95 and other cases on which the Supreme Court of Georgia rests its decision are inapplicable.

III

The history of the previous litigation in the Supreme Court of the United States, construing the Charter of the Georgia Railroad, and kindred Charters.

Many railroads were chartered by the Legislature of Georgia (prior to the Code of January 1, 1868, which prohibited the grant of irrevocable charters) which had tax limitations of ½ of 1% on their net income. All of these Companies have passed out of existence except three—Georgia Railroad and Banking Company, Augusta and Savannah Railroad, and South Western Railroad Company, the railroads of the two latter being leased by Central of Georgia Railway Company.

All railroads in Georgia, whether they had Charter tax limitations or not, were commonly taxed at the rate of ½ of 1% on their net incomes,* until the Act of February 28, 1874, (Acts of 1874, p. 107), the title of which Act is "An Act to amend the tax laws of this State so far as the same relate to railroad companies, and to define the liabilities of such companies to taxation, and to repeal so much of the Charters of such companies, respectively, as may conflict with the

*Act Dec. 11, 1858, Sec. 8, p. 104; Act Dec. 14, 1861, Sec. [illegible] p. 80; Act 1868, p. 143; Act Oct. 5, 1863, Sec. 3, p. 154; Act March 15, 1869, p. 160; Act Jan. 19, 1872, Sec. 3, p. 276; Act February 20, 1873, p. 65; Act, Feb. 28, 1874, Sec. 3, p. 103.

provisions of this Act". This Act provides that the railroads should be taxed as other property of the people of the State, (Codified, except as to title, Code of Georgia Ann., Secs. 92-2602, 2603). This Act brought on all the litigation over these Georgia railroad Charters which subsequently ensued.

There have been several cases decided by the Supreme Court of the United States holding these Charters to be irrevocable contracts,[1] and there have been two cases construing the Charter of the Georgia Railroad and two cases construing the Charters of the Augusta and Savannah Railroad and the South Western Railroad, which are specially applicable here.[2]

In *Wright* v. *Georgia Railroad & Banking Company*, 216 U.S. 420, affirming 132 F. 912, the State of Georgia was trying to tax the Georgia Railroad with a franchise tax, and was also trying to tax the Railroad Company with the increased value of its property due to additions and betterments. The Court held in this case, that the attempted tax would violate the Charter of the Company, that its property was exempt from taxation, and that it was not subject to any form of taxation except the tax of ½ of 1% on the net income, and that this tax would exhaust the power of the State to tax.

The cases of *Wright* v. *Louisville & Nashville Railroad Co., et al.*, 236 U.S. 687, affirming 199 F. 454,

1 Central Railroad & Banking Co. v. Georgia, 92 U. S. 655; South Western Railroad Co. v. Georgia, 92 U. S. 676; South Western Railroad Co. v. Wright, 116 U. S. 231.

2 Wright v. Georgia Railroad & Banking Co., 216 U. S. 420, affirming 132 F. 912; Louisville & Nashville Railroad Co., et al. v. Wright, 236 U. S. 687, affirming 199 F. 454, and 201 F. 1023; Wright v. Central of Georgia Railway Co., 236 U. S. 674, affirming 206 F. 107; Central of Georgia Railway Company v. Wright, 248 U. S. 525, reversing 146 Ga. 406; re-hearing granted 249 U. S. 590; decision on Re-hearing 250 U.S. 519.

and 201 F. 1023, and *Wright* v. *Central of Georgia Railway Company*, 236 U.S. 674, affirming 206 F. 107, were companion cases. Central of Georgia Railway Company was the Lessee of Augusta and Savannah Railroad and South Western Railroad which had Charter tax limitations similar to that of the Georgia Railroad. The Lessors were not parties to these cases. The contention in both cases was that the Lessees had long term leases and were the virtual owners of the properties, in view of which the State attempted to tax the Lessees with the fee of the properties. In both cases the Supreme Court dwelt on the power to lease contained in the Georgia Charter and contained in the Augusta and Savannah Charter, and the Court held in the Central of Georgia case (p. 679) that "No change in the manner of tax exemption was expected to follow from the demise of the road, any more than it would have followed from the admission of another carrier to partial rights or of an individual to carry his own goods", and made the same observation in the Georgia Railroad Charter case (p. 689). These two cases did not turn on the Fourteenth Amendment. They held specifically that the Lessees were protected by the Charter and that the Charter inured to the Lessees; and that the Railroad already had been exhaustively taxed in the manner pointed out by the Charter, and the Charter contract prevented the fee from being taxed to the Lessees. In the motion to dismiss or affirm, attention is called to the decree rendered by Judge Newman in the United States Circuit Court, who held that the Georgia Railroad lease created merely the relation of landlord and tenant and did not vest in the Lessees any estate. The State contended that the leases did create estates in the Lessees, but the

Supreme Court of the United States brushed this question aside and decided the case without any relevancy to whether the lease was a mere usufruct or an estate.

These two cases involving the taxation of the fee to the Lessees were followed by the case of *Central of Georgia Railway Company* v. *Wright*, 248 U.S. 525, reversing 146 Ga. 406. The contention in this case was that the leasehold interest of the Central of Georgia Railway Company in the Augusta and Savannah Railroad and in South Western Railroad Company was property under the laws of Georgia, and was taxable as property. The Court decided in this case (p. 526) that the case "presents another attempt to accomplish, by a change in form, what in Wright v. Central of Georgia Railway Company, 236 U.S. 674, was held to be an unconstitutional result", and that the Lessee was protected by the Charter from being taxed with the leasehold interest, although the leasehold interest was property of the Lessee. A re-hearing was granted in this case, *Central of Georgia Railway Company* v. *Wright*, 249 U.S. 590, as to the charter tax under the Charter of the South Western Railroad. On the rehearing, *Central of Georgia Railway Company* v. *Wright*, 250 U.S. 519, the Court re-affirmed its decision in 248 U.S. 525 as to the South Western Railroad.

This case concluded any attempt on the part of the State to tax the Atlantic Coast Line Railroad Company and the Louisville & Nashville Railroad Company, as Lessees of the Georgia Railroad, with their leasehold interest, because the situation in the Georgia Railroad leases was exactly the same as the situation in the Augusta and Savannah and South Western Railroad Company leases. If the leasehold interest

was not taxable to the Lessees and if they were protected by the Charter from being taxed ad valorem on the leasehold interest, it follows, a fortiori, that they cannot be taxed 5½% on the income from the leasehold interest.

This case is a part of a studied purpose of the taxing authorities of the State of Georgia to avoid and evade the Charter tax limitations of the Charters of the Georgia Railroad and Banking Company, Augusta and Savannah Railroad and South Western Railroad Company. The State is now proposing to tax the Georgia Railroad and Banking Company, the Augusta & Savannah Railroad, and the South Western Railroad on their properties on the ad valorem basis, just as though the Charter tax limitations had never existed. (T.R. 93, 94). The State also proposes to tax the Georgia Railroad and Banking Company (T.R. 85), Augusta and Savannah Railroad (T.R. 82), and the South Western Railroad (T.R. 89), 5½% on their respective rentals, in addition to the Charter tax of ½ of 1% on the net income of the Charter tax lines.

IV

It has been the invariable practice for more than 100 years to tax the net income of the Charter tax Lines and not the rentals paid by the Lessee.

In *Goldsmith v. Augusta and Savannah Railroad*, 62 Ga. 468, it was held (p. 472) "the income contemplated by the Charter is not the annual rental, but the earnings of the road".

In *Georgia R.R. & Bkg. Co. v. Wright*, 132 Fed. 912, Judge Newman said "The State has for sixty years or more allowed the Company to return its net

earnings and pay a tax thereon of one-half of 1% without objection". See also evidence of H. E. Judge (T.R. 56, 57).

The point in this contention is that, under the Charter, the thing which is taxed is not the income of the Georgia Railroad, but the net income of the operations of the Charter tax lines. The scheme of the Charter as interpreted both by the Supreme Court of Georgia and by this Court is that the net income of the Charter tax lines should be taxed no matter who earned it, whether Lessor or Lessee, and that when this tax is paid, the power of the State to tax further or differently to either Lessor or Lessee is exhausted.

V

Under the Georgia Railroad Charter the tax is levied exclusively on the net income of the Charter tax lines. The property is exempt from taxation. When the tax of ½ of 1% is levied, the power of the State to tax further is exhausted.

In *Georgia Railroad & Bkg. Co.* v. *Wright*, 132 F. 912, Judge Newman held (p. 919): "It is clear that it was the intention of the Legislature to provide a full and complete system of taxation for this corporation, and that it embraces its whole liability for taxation."

In *Wright* v. *Georgia Railroad & Bkg. Co.*, 216 U.S. 420, which affirmed Judge Newman's decision in 132 F. 912, the Court held:

> (p. 426) "That the only mode of taxation stipulated for after the period of total exemption is a tax upon the net income of the company's property is seemingly the plain and obvious meaning of this contract. That this is the way

in which it has been read and interpreted by everybody who has had to do with the matter of taxation in an official way since 1845, when the railroad seems to have been finished, affords strong evidence that this construction accords with the intent of the charter."

(p. 430) "After all, the precise question is, whether the legislative purpose, as expressed, was that the railroad incorporated should pay no tax except one based upon net profits of operation, or was it the intention that a specific amount of capital only should be so relieved? Undoubtedly, the State did not intend that any other capital than that authorized and invested directly in this specific railroad should be immune. That is plain by the express limitation of the charter. But is there any contingency under which this particular railroad is to be subject to any other taxation than one measured by the amount of its net profits?"

(pp. 431, 432) "This plan of tax upon net earnings is quite inconsistent with any other form of taxation, and is absolutely independent of any question as to whether the property thus taxed only upon its profits should have a less or greater value than the capital invested. A tax upon earnings is a tax which at last covers and includes, unless double taxation is intended, all property necessarily held and used to make that income, including the enjoyment of its franchises. It is not to be presumed, in the light of the public policy of the time, that the State intended that this pioneer railroad should be subjected to any form of taxation of property which produced the taxable income * * * We are, therefore of opinion that this property is not subject to any other method of taxation than that of the special system stipulated for by the contract, and that the act of the Georgia Legis-

lature, in so far as it provides for an ad valorem tax upon any part of this invested capital of the Georgia Railroad and Banking Company, does impair the obligation of the contract."

(p. 432) "If we are right in construing the tax as one upon net income as a substitute for a property tax, the franchise may no more be taxed than any other property appropriate to the operation of the road. When the State gave up the right to levy and collect a property tax and to take in substitution a tax upon the annual net profit, it gave up the right to tax the franchise of the company as certainly as it gave up the right to tax its railroad."

(page 436) The Court, in referring to the tax limitation of the Charter, describes it as "the immunity from any other tax than one based upon a given per cent. of annual net profits".

VI

The Contract Inures to the Lessees.

The Charter is an umbrella over the Lessees as well as the Lessor. When the tax of one-half of one per cent is paid on the net income, the power of the State to tax is exhausted. We wish to emphasize the fact that the thing which is taxed is the net income yielded by the Charter tax lines, whether that income is made by the operations of the Lessor or Lessees.

The protection of the Lessee is necessary to make good that promised the Lessor. Manifestly if the Lessee is not protected by the Charter the Lessor's ability to rent its property is materially affected. If the State can tax the same net income which has already been

taxed under the Charter one-half of one per cent, another .5½% under the Income Tax Act that which is promised the Lessor is denied; although the 5½% tax may be paid by the Lessee, because the Lessee took the lease on the faith of the contract. The State cannot double tax without violating the Charter.

In *Wright* v. *Louisville & Nashville Railroad Co., et al.*, 236 U.S. 687, which involved the question whether the State could tax the Lessees with the fee of the property, the Court first called attention to the fact that the 12th Section of the Charter of the Georgia Railroad authorized it to rent the whole or any part of its property or to let vehicles of others pass over its railroad, and the Court then said (p. 689) "So that the State has covenanted that the Company's property shall be exempt from tax except upon its income *which it is authorized to make in any of those ways* (Italics ours) * * * For the reasons given in the other case (Wright v. Central of Ga. Ry. Co., 236 U.S. 674), we cannot believe that if the Company saw fit to gain 'the net proceeds of their investments' (to one-half of one percent of which their tax was limited), by letting the whole road instead of allowing others to introduce carriages, *the Statute silently opened the right to resume as against the Lessee all that had been removed as against the Lessor*" (Italics ours). And again at page 690 the Court said: "If the fee of the roads is taxable to no one while the liability of the Lessor to the above mentioned one-half of one per cent, remains, an attempt to collect a tax upon the fee from the plaintiffs is an attempt on the part of the State to tax the leased property which was completely beyond the reach of its taxing power except in so far as

permitted by the contract, the obligations of which could not be impaired without a violation of the contract clause of the Constitution of the United States."

In the companion case of *Wright v. Central of Georgia Railway Co.*, 236 U.S. 674, which involved the taxation of the fee of the Augusta and Savannah and South Western Railroads, to their Lessee, Central of Georgia Railway Company, the Court said (p. 679):

> "The foregoing view of Section 16 would lead us to believe that no change in the matter of tax exemption was expected to follow from the demise of the road, any more than it would have followed from the admission of another carrier to partial rights, or of an individual to carry his own goods. But that is only an introduction to further considerations. We cannot suppose that the Legislature meant either to practice a cunning deception or to make a futile grant. Therefore, we are unable to read the charter as making the exemption vain by reserving to the State an unlimited right to impose upon the Lessee all that it had renounced as against the lessor. For that was to give notice to the parties, if they were supposed to know the law, that the exemption would be lost if the income was earned in one of the contemplated ways—or, if they were supposed ignorant, was to invite them to a bargain that was to have an unexpected and disastrous result."

And again the Supreme Court held on pages 679 and 680:

> "We see no ground for believing that there has been any change in the attitude of the State toward the pioneer enterprises that it was en-

couraging a few years before. We still cannot suppose that it was inviting the lessors to lose the benefit of their exemption or the lessees to find themselves entrapped with a burden made possible only by accepting the invitation of the act * * * We construe those statutes as making the fee exempt from other taxation than that provided for, in favor as well of the lessee as of the lessor—the protection of the lessee being necessary in order to make good that promised to the lessor".

In *Central of Georgia Railway Company* v. *Wright*, 248 U.S. 525, in which the State attempted to tax Central of Georgia Railway Company with its leasehold interest in the Augusta and Savannah Railroad and the South Western Railroad Company, the Supreme Court said (h.n.1):

"The same reasons which lead this Court to decide that the tax exemptions in the special charters of the Augusta and Savannah and the South Western Railroads inured to the Central of Georgia Railway as their lessee and precluded taxing the latter upon the fee of the leased property (Wright v. Central of Georgia Ry. Co., 236 U.S. 674) invalidate an attempt to evade the charter contracts by a tax of the leasehold interests."

In the body of the opinion the Supreme Court referred to the fact that the previous case in 236 U.S. 674 was an attempt to tax the Lessees with the fee of the two leased lines. In the course of its opinion, the Court said, (p. 527):

"The taxes now attempted to be levied are upon the leasehold interests of the Lessee in the same roads and it is argued that, if the leases produce a profit in excess of the rental, the

value is required to be taxed by the Constitution of the State. But the Constitution was subsequent to the charters that created the exemption and must yield to them if they apply to the present attempt. We are of opinion that, although the decision in the former case necessarily was confined to the question before the court, the reasoning applies with equal force to that now before us. The cases of Rochester Ry Co. v. Rochester, 205 U.S. 236, and Jetton v. University of the South, 208 U.S. 489, were urged as opposed to the conclusion reached but were thought not to control in view of the exceptional facts and language that had to be considered, as was recognized in Morris Canal & Banking Co. v. Baird, 239 U.S. 126, 132. We must follow the precedent that was established after full discussion and with recognition of the difficulties involved."

A re-hearing was granted in *Central of Georgia Railway Co.* v. *Wright*, 249 U.S. 599, as to the South Western Railroad, and in *Central of Ga. Ry. Co.* v. *Wright*, 250 U.S. 519, the decision as to the South Western Railroad in 248 U.S. was re-affirmed.

The decision of the Supreme Court of Georgia in *Wright* v. *Central of Ga. Ry. Co.*, 146 Ga. 406, which was reversed in *Central of Georgia Ry. Co.* v. *Wright*, 248 U.S. 525, and 250 U.S. 519, set at rest the question that a leasehold interest under the law of Georgia was property in the hands of the Lessee, and under the Constituiton of the State of Georgia it was taxable to the Lessee. If the Charter is protection to the Lessee against taxing the Lessee with its separate property interests in its leasehold, then why is not the Charter a protection to taxing the Lessee 5½% on the income

from the Charter tax lines under the Income Tax Act of March 31, 1931? For the very same reason that the leasehold is protected by the Charter, the income derived from the Charter tax lines covered by the lease is, a fortiori, protected.

The leasing powers in the Georgia Railroad Charter are substantially similar to the leasing powers in the Augusta and Savannah Railroad Charter. The State of Georgia was concluded by the decision in 248 U.S. 525 from attempting to tax the leasehold interest of the Lessees of the Georgia Railroad, because precisely the same questions were involved. So that the cases in 248 U.S. 525 and 250 U.S. 519 are authority in this case, which was binding on the Supreme Court of the State of Georgia.

VII

It makes no difference whether the Charter Tax is construed as a Property Tax or as an Income Tax, in either event the Charter is impaired by taxing the net income from the Charter tax lines to the Lessor or the Lessees at 5½% under the Income Tax Act of 1931.

We have demonstrated that under the Charter the property is exempt from taxation, that the income under the Charter cannot be taxed higher than ½ of 1%, that the Charter inures to the Lessees, that the leasehold interest of the Lessees cannot be taxed to the Lessees without violating the Charter, and that all of these questions have been definitely decided by this Court. We maintain that it logically and necessarily follows that the net income from the Charter tax lines cannot be further taxed 5½% to the Lessees without violating the Charter.

Just why it should violate the Charter to tax the leasehold interest to the Lessees and not violate the Charter to tax to the Lessees the income from the leasehold is impossible to explain. It does not make any difference whether the tax levied under the Charter is defined as a property tax or an income tax, the impairment of the Charter is the same in substance, kind and extent.

We understand, of course, that a person can be taxed on his property and at the same time taxed on the income from the same property, and that although this may be double taxation, that it is legally permissible, because there is no statute or constitutional provision against double taxation. But here we are dealing with a contract. The State cannot tax the Georgia Railroad ½ of 1% under the Charter and then tax the Georgia Railroad 5½% in addition under the Income Tax Act of 1931. The Charter prohibits a tax *higher* than ½ of 1%.

If we are right in the proposition that the Charter tax provision inures to the Lessees (as has been decided by this Court), then it makes no difference whether the Charter tax is a property tax or an income tax, because the result is that the net income under the Charter, whether earned by the Lessor or the Lessees can not be taxed higher than ½ of 1%.

VIII

The Charter Tax is not a Property Tax. It is an Income Tax.

The Supreme Court of the State of Georgia in this case has defined the charter tax as a property tax and, having so defined it, it then asserts that an income tax was unknown in the State of Georgia at the time this

charter was granted in 1833 and therefore it was not the intention of the Legislature that the income from the charter tax lines should not be taxed. All this was to bring the case within the decision by the Supreme Court of the United States in *Hale* v. *State Board*, 302 U.S. 95, which we distinguish hereinafter.

But the charter lays the tax specifically on income. The charter in terms designates the tax an an income tax. Therefore, no room is left for the decision of the Supreme Court of Georgia that the charter tax is a property tax. Income may be derived from physical property, or from securities, or from individual effort, or it may be derived from the use of physical property. The income tax imposed by the Georgia Railroad charter contemplated that the Railroad would be worked by someone and that the net proceeds of its operation was the thing which the charter aimed to tax. The fact that the income is made from property does not make the tax thereon a property tax. When the charter of the Georgia Railroad was written, in referring to income, necessarily the income spoken of was the income of particular property. We have already pointed out the significance that the income which is taxed under this charter is not necessarily the income of the Georgia Railroad & Banking Company. This Court has decided that the income might be made by either the lessor or lessee and that the demise of the railroad did not effect the charter tax.

This Court has decided specifically that the property is exempt from tax and that the only tax which can be levied is ½ of 1% on the net income, and that this is the exclusive mode of taxation.

In the case of *Featherstone* v. *Norman*, 170 Ga. 370, the Court held that income was not property in the sense in which that term is used in the Constitution of the State, requiring all property to be taxed uniformly. The Court said (at p. 393): "So both the property from which the income comes, and the income itself, are subject to separate assessments for taxation. The two are separate and distinct things. The taxation of one is not the taxation of the other. The assertion that the tax on one is a tax on the other is a fanciful conceit to which we cannot agree." This quotation fits our case. We say it is a fanciful conceit to say that the charter tax of ½ of 1% is a property tax and not an income tax.

In *Wright* v. *Georgia Railroad & Banking Company*, 216 U.S. 420, this Court, after deciding explicitly that the property of the Georgia Railroad was exempt from taxation, and that the only method of taxation under the charter was a tax on net income, said (at p. 432): "If we are right in construing the tax as one upon net income as a substitute for a property tax, the franchise may no more be taxed than any other property appropriate to the operation of the road. When the State gave up the right to levy and collect a property tax and to take in substitute a tax upon the annual net profit, it gave up the right to tax the franchise of the Company as certainly as it gave up the right to tax its railroad."

If the Charter tax on income is a substitute for a property tax, then it clearly is not a property tax. It could not at the same time be a property tax and a substitute for a property tax. What this Court meant

when it said that the net income tax was a substitute for a property tax was that although property is generally taxed in this State, instead of taxing the property the Legislature elected to tax the income.

Income is itself property, but a tax on income is commonly defined as an income tax, although the income may be derived from the use or operation of property. "A tax upon earnings is a tax which at last covers and includes, unless double taxation is intended, all property necessarily held or used to make that income" (*Wright* v. *Georgia Railroad & Banking Co.*, 216 U.S. 420, 432). "A tax on the income from land is not a tax on the land itself" (*Cohn* v. *Graves*, 300 U.S. 308, h.n. 6).

It is argued that the Charter tax of ½ of 1% is a *measure* of the tax on the property, hence the tax is a property tax. It may be a tax levied in lieu of a property tax, but that does not make it a property tax. At the time this Charter was passed there was no constitutional provision requiring a property tax. The best evidence that this Charter tax is not a property tax is the decision of this Court holding that the increment of the market value of the property, due to additions and betterments and other causes, is not taxable under this Charter. (*Wright* v. *Georgia R.R. & Bkg. Co.*, 216 U.S. 420, 427-432).

There is a long line of cases decided by this Court which hold that a franchise or privilege tax may be *measured* by the entire income, although some of the income is derived from taxable property, as, for instance, *Flint* v. *Stone Tracy Co.*, 220 U.S. 108; *Society*

for Savings v. *Corte*, 6 Wall. 594; *Provident Institution* v. *Mass.*, 6 Wall. 611; *Home Ins. Co.*, v. *New York*, 134 U.S., 594; *Pacific Co.* v. *Johnson*, 285 U.S. 481.

But the Income Tax Act of March 31, 1931, under which the State Revenue Commission is proceeding is not a franchise or a privilege tax. It is a direct tax on the income of all persons. Under this Act, the net income is not the measure of the tax, the net income is the thing taxed.

IX

Rochester Railway v. Rochester, 205 U. S. 236, and kindred cases, distinguished.

There is no transfer or assignment of the property in this case; it is merely a case of lease authorized by the Charter.

The Supreme Court of the United States has held in the cases hereinbefore cited, that under the peculiar provisions of these Georgia Charters granting tax limitations, the demise of the railroads to the lessees did not affect the charter limitations, and that they inured to the lessees, and in its opinions distinguished the cases of:

Rochester Ry. v. *Rochester*, 205 U.S. 236.

Jetton v. *University of the South*, 208 U.S. 439.

Morris Canal Co. v. *Baird*, 239 U.S. 126.

The Rochester case and the Morris Canal Company case both decided that the grant of immunity from taxation was personal to the owner of the property to whom the immunity was granted, and the immunity

could not be transferred. The Supreme Court in *Wright v. Louisville & Nashville R.R. et. al.*, 236 U.S. 687, 690, (which involved the taxation of the Georgia Railroad to the Lessees), said:

> "Thus the particular features of the case in hand take it without the rule applied in Rochester Railway v. Rochester, 205 U.S. 236, and other kindred cases, from which we have no purpose to depart."

In *Central of Georgia Railway Company v. Wright*, 248 U.S. 525, 526 (which was a case which involved taxing the leasehold interests of the Central in the Augusta and Savannah and the South Western Railroads), the Court said:

> "The cases of Rochester Ry. Co. v Rochester, 205 U.S. 236, and Jetton v. University of the South, 208 U.S. 489, were urged as opposed to the conclusion reached but were thought not to control in view of the exceptional facts and language that had to be considered, as was recognized in Morris Canal & Banking Co. v. Baird, 239 U.S. 126, 132."

In *Morris Canal Co. v. Baird*, 239 U.S. 126, 132, the Court said, after citing the case of *Rochester Ry. Co. v. Rochester*, 205 U.S. 236:

> "The results in Wright v. Central of Georgia Ry., 236 U.S. 674, and Wright v. Louisville & Nashville R.R. Co., 236 U.S. 687, 690, were based upon the original charters, which were interpreted as contemplating and permitting subsequent transfers without subjecting the fee to taxation. Neither of these cases modifies the

principles announced and applied in the opinion quoted from above—it is referred to with approval in the latter of them."

The fact that the Supreme Court of the United States in the case in 248 U.S. 525 held that the case of *Jetton* v. *University of the South*, 208 U.S. 489, was not controlling, is significant. In the University of the South case, the exemption from taxation was "as long as said lands belong to said University". The University leased the lands and it was held that the leasehold interest was taxable to the Lessee as property separate and distinct from the fee of the University, which was still protected by the Charter exemption. In the case at bar, as in the case of Central of Georgia Railway Company, decided in 248 U.S. 525, the tax limitation protected the Lessee as well as the Company which owned the railroad, because all interest in the property was taxed when the Charter rate was paid on the net income, the power of the State being exhausted.

X

The Contract is impaired if its value is diminished or if it is affected at all.

"One of the tests that a contract has been impaired is that its value has by legislation been diminished. The applicable section of the Constitution of the United States provides that the contract shall not be impaired at all. It is not a question of degree; manner, or cause, but one of whether the subsequent legislation of the state encroaches in any respect on the obligation of the contract or dispenses with any part of its force."

Norfolk & W. Ry. Co. v. *Boyle*, 12 F. Supp. 522, 523.

"The amount of the impairment of the obligation is immaterial. If there be any, it is sufficient to bring into activity the constitutional provision and the judicial power of this Court to redress the wrong."

Farrington v. *Tennessee*, 95 U.S. 679, 683.

"The prohibition has no reference to the degree of impairment. The largest and least are alike forbidden. In Green v. Biddle (8 Wheaton 84), it was said: 'The objection to a law on the ground of its impairing the obligation of a contract can never depend upon the extent of the change which the law effects in it. Any deviation from its term by postponing or accelerating the period of performance which it prescribes, imposing conditions not expressed in the contract, or dispensing with those which are, however minute or apparently immaterial in their effect upon the contract of the parties, impairs its obligation."

Van Hoffman v. *City of Quincy*, 4 Wall, 535, 552, 553.

"The objection to a law, on the ground that it impairs the obligation of a contract, does not depend upon the extent of the change which the law may make in it." (h.n.2).

"Any deviation from its terms, by imposing conditions not expressed in the contract, however minute, and apparently immaterial in their effect, is within this constitutional prohibition." (h.n.3).

Winter v. *Jones*, 10 Ga. 190.

XI

The Supreme Court of Georgia did not follow the construction put by the Supreme Court of the United States on this and kindred charters.

The decisions of the Supreme Court of the United States construing a contract to determine whether subsequent legislation is violative of its provisions in view of the Contract Clause of the Federal Constitution are controlling on the Supreme Court of Georgia. No one doubts this proposition. The Supreme Court of the United States leans to accept the construction of such a charter by the State Courts unless the construction of the State Court is manifestly wrong. But when the Supreme Court has construed such a contract, the Supreme Court of the State is not at liberty to put a different construction on the contract. But that is just what the Supreme Court of Georgia has done in this case. The Supreme Court of Georgia says in its decision (T. R. 116): "We are not unmindful of certain language of the Federal Courts indicating that those courts regarded the tax referred to in this charter provision as an income tax". And then the Supreme Court of Georgia in utter disregard of the plain specific decisions of the Supreme Court of the United States proceeds to construe the contract contrary to the decisions of the Supreme Court of the United States.

The construction of the charter tax as a property tax is definitely contrary to the constructions put on this charter by the Supreme Court of the United States. If the Supreme Court of Georgia had followed the construction put on this charter and the kindred charters of the Augusta & Savannah and the South Western Railroads, the Supreme Court of Georgia could

not logically uphold the income tax assessment in this case. But the Supreme Court of Georgia in order to bring the case within the orbit of Hale vs. State Board, Supra., defined the charter tax as a property tax and then finds that as income taxes were unknown to Georgia when this charter was passed in 1833, that there is no charter obstruction to the assessment on the lessee of the 5½% income tax under the Act of 1931. We hereafter challenge the finding that income taxes were unknown in the State of Georgia when this charter was granted.

The decisions of this Court on the power of the Court to construe a contract to determine whether subsequent legislation violates the contract clause of the Federal Constitution is epitomized in the following decision:

> "This Court, in construing a contract to determine whether or not legislation is violative of its provisions within the meaning of the contract clause of the Constitution, will examine for itself the existence and meaning of the contract as well as the relation of the parties and the circumstances of its execution. Appleby v. City of New York, 271 U.S. 364, 379-380; Funkhouser v. Preston Co., 290 U.S. 163, 167; Violet Trapping Co. v. Grace, 297 U.S. 119, 120. But of course in doing so we 'lean toward agreement with the courts of the state, and accept their judgments as to such matters unless manifestly wrong', Hale v. State Board, 302 U.S. 95, 101; Tampa Water Works Co. v. Tampa, 199 U.S. 241, 243-244; Southern Wisconsin Ry. Co. v. Madison, 240 U.S. 457, 461."

Rapid Transit Corp. v. *New York*, 303 U.S. 578.

XII

Income taxes were not unknown in the State of Georgia when this Charter was passed. All railroads were habitually taxed one-half of 1% on their net income until the year 1874.

The Supreme Court of Georgia in its decision (T.R. 116) states "A number of railroad charters existing at the time or subsequently granted, contained similar provisions for taxation, but there existed in this State at that time no general law providing for income taxes. It was almost a century thereafter before the Legislature enacted our present income tax statute". It is true that there was no general law providing for income taxes in Georgia in 1833. The Constitution of Georgia of 1798 was the Constitution in effect when this Charter was passed. There was no provision in this Constitution or any subsequent Constitution of the State of Georgia until 1868 as to uniformity of taxation. Nor was there any requirement that property should be taxed ad valorem or in any other particular manner. When the Georgia Railroad Charter was passed, the tax imposed was an income tax. Therefore, it is preposterous to argue that income taxes were unknown in the State of Georgia at this time, or that the Legislature did not know what it was doing when it imposed an income tax rather than a property tax. As stated in the decisions of the Supreme Court, there were a number of railroads chartered by the State of Georgia which had charter limitations of one-half of 1% on net income. There were a number of other railroads chartered which had no tax limitations. The decision of the Supreme Court of Georgia (T.R. 118), refers to the decision of Mayor, etc. of Savannah v. Hartridge, 8 Ga. 23, which draws a distinction between

income taxes and property taxes. This case arose in 1849. The Supreme Court says in connection with this case in 8 Ga. 23 (T.R. 119) "* * * while that decision was rendered several years after the enactment of the Charter here involved, it must be assumed that the Legislature, when enacting this Charter, was acquainted with the fact as there recited that 'writers on political economy as well as the tax laws of all governments' thus divided the forms of taxation and adhered to the rule that where one or more forms of taxation are treated or acted upon the other was never intended." So that according to the decision of the Supreme Court of Georgia, the Legislature did know the distinction between income taxes and property taxes, and knowing the distinction it advisedly imposed an income tax under the Georgia Railroad Charter.

As early as 1858 and down to 1874, all railroads in Georgia, whether they had charter tax limitations or not, were commonly taxed at the rate of ½ of 1% on their net incomes (see the Statutes collected in a footnote on page 6 of this brief).

But we maintain, as elsewhere set forth in this brief, that it makes no difference whether the Charter tax was an income tax or a property tax, an additional tax under this Charter cannot be imposed either on the Lessor or the Lessees.

XIII

The case of Hale v. State Board, 302 U.S. 95, distinguished

This is the case on which the Supreme Court mainly rests its decision. It is wholly unlike the case at bar.

In the Hale case, under the Statutes of Iowa certain bonds were exempt from taxation and the Court

assumed that the Statutes constituted a contract. The Supreme Court of Iowa construing these Statutes held that the bonds were exempt, but that the income on the bonds was not exempt because at the time the Statutes were passed there was no general income tax law in Iowa. The Supreme Court of the United States elected to follow the decision of the Supreme Court of Iowa, although it was not bound to do so. The same argument cannot be made in the case at bar, because under the Georgia Railroad Charter the tax is specifically an income tax and the Supreme Court of the United States has held that under the Georgia Railroad Charter the property is exempt from tax. The Supreme Court of the United States has also held that no other mode or method of taxation, except the income tax, can be imposed under this Charter, and as no higher tax than one-half of 1% can be imposed, this tax when imposed is exhaustive of the power of the State.

While there was no general income tax statute in Georgia when this Charter was passed, the Legislature, as the Supreme Court of Georgia has said, must be presumed to have been familiar with the general subject. Certainly it would be a violent assumption to suppose that the Legislature imposed the income tax in ignorance of what it was doing.

Moreover, all railroads in Georgia were habitually taxed ½ of 1% on their net income, whether they had a charter contract or not, until 1874, when the method of taxing railroads was changed to a tax on their property ad valorem.

If in the Hale case the holders of the bonds were taxed under a statute of Iowa ½ of 1% on the income

of the bonds, and this statute was a contract, an additional tax of 5½% could not have been imposed under a subsequent general income tax act. That is exactly the case here.

In *Wright* v. *Georgia Railroad & Bkg. Co.*, 216 U.S. 420, the State was seeking to tax the Georgia Railroad with a Franchise Tax Act which was passed in 1902 (Acts 1902, p. 37). There never had been any franchise tax in Georgia before this. In 54 Lawyers' Co-Operative Ed. p. 548, where this case is reported, the argument of John C. Hart and Samuel H. Sibley, representing Comptroller General Wright, is quoted as follows: "The fact that a franchise had never been taxed when the stipulations were made may explain why no agreement was made respecting it, but does not operate to hinder bringing within the power of taxation the new subject matter". The Supreme Court of the United States brushed this argument aside. If the new franchise tax could not be imposed without violating the Charter, a fortiori, the new income tax of 1931 cannot be imposed without violating the Charter.

But, as we have argued elsewhere in this brief, it makes no difference whether the Charter tax is a property tax or an income tax, the tax having been imposed under the Charter up to the maximum, no other or additional tax whatever it may be called, can be imposed.

XIV

Other cases cited by the Supreme Court of Georgia and by Appellee in its motion to dismiss or affirm, distinguished.

Clyde v. *Gilchrist*, 262 U.S. 94.

Adams Mfg. Co. v. *Storen*, 304 U.S. 307.

These two cases are similar to the case of *Hale* v. *State Board*, 302 U.S. 95, and are inapplicable for the same reasons set forth in the preceding point, which distinguishes that case.

Ex rel. *Cohn* v. *Graves*, 300 U.S. 308.

This case decides that "a State may tax her citizen upon the income he receives by way of rents from lands situate in another State and by way of interest on bonds secured by mortgage on lands situate in another State"; and it also decides that "a tax on the income from land is not a tax on the land". The first proposition is irrelevant and the last proposition supports our argument that the tax in this case is not a property tax.

Mason Co. v. *Tax Com. of Washington*, 302 U.S. 186.

This case merely decides that "a State Occupation Tax on gross receipts may constitutionally include the receipts from construction work done under a contract with the United States". There were only two questions in this case—one, whether the tax imposes an unconstitutional burden upon the Federal Government; and the other was, whether the area in which the work was performed was within the exclusive jurisdiction of the United States. This case does not seem to touch the case at bar.

Adams v. *Saenger*, 303 U.S. 59.

This case involved a question of what effect should be given in one State to the judgment of another State. The citation was probably a mistake.

Helvering v. *Bankline Oil Co.*, 303 U.S. 362.

Graves v. *O'Keefe*, 306 U.S. 466.

The first case involved the question whether a Federal tax on the profits from land leased from the State was invalid as an unconstitutional burden on a State instrumentality, and the second case involved the question whether the State of New York could tax the salary of a New York resident earned as Attorney for the Federal Home Owners Loan Corporation, which was a Federal instrumentality. These cases do not seem to remotely touch the case at bar.

New York Rapid Transit Corp. v. *State of N. Y.*, 303 U.S. 573.

In this case a privilege tax of 3% on gross income was imposed on the New York Rapid Transit Corporation. The question was whether this tax violated the contract of this corporation with the City of New York. The Court said on page 590: "We searched in vain for any provision in the contract which expressly exempts the corporation from the payment of this tax or indeed any tax", and again on page 591 the Court said "Not only is the corporation unable to point to an unmistakable exemption, but the contract itself contains an express provision permitting the deduction of taxes from the gross receipts".

U. S. Trust Co. v. *Helvering*, 307 U.S. 57.

This case is wholly irrevelant. The only question in the case was whether the proceeds of a war risk insurance policy payable to a soldier's widow should be included as a part of the soldier's gross estate for purposes of Federal estate taxes.

XV

Conclusion.

We think we have demonstrated the proposition that the position of the Appellee "that the questions on which the decision of the cause depends are so unsubstantial as not to need further argument" (Rule 7 (4)), is not well taken. Moreover, we think that we have demonstrated that the judgment of the Supreme Court of Georgia should be reversed.

Respectfully submitted,

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August 6, 1946.

APPENDIX I

Extract from Sections 12 and 14 of Charter of Georgia Railroad Company (Acts 1833 pp. 262, 263).

Sec. 12 * * * "that the said company may, when they see fit, rent or farm out all or any part of their said exclusive right of transportation or conveyance of persons on the rail-road or rail-roads, with the privilege to any individual or individuals, or other company, and for such term as may be agreed upon, subject to the rates above mentioned. And the said company, in the exercise of their right of carriage or transportation of persons or property, or the persons so taking from the company the right of transportation or conveyance, shall, so far as they act on the same, be regarded as common carriers." * * *

Sec. 14 * * * "That whenever the company aforesaid shall see fit to farm out as aforesaid, to any person or persons, or body corporate, any part of their exclusive right of conveyance and transportation, or shall deem it expedient to open the said road or any part thereof, to public use, they shall and may adopt and enforce all necessary rules and regulations, and have power to prescribe the construction and size or burthen of all carriages and vehicles, and the materials of which such shall be made, that shall be permitted to be used or pass on the said rail road, and the locomotive power that shall be used with them." * * *